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IN THE COURT OF APPEAL OF THE STATE OF CALIFORNIA

FOURTH APPELLATE DISTRICT

DIVISION THREE

MICHELLE'S DIAMOND LLC et al.,

Plaintiffs and Respondents,

v.

REMINGTON FINANCIAL GROUP,
INC., et al.,

Defendants and Appellants.

G040163

(Super. Ct. No. 07CC08380)

O P I N I O N

Appeal from an order of the Superior Court of Orange County, William M. Monroe, Judge. Affirmed.

Kutak Rock, Steven M. Dailey and Chris D. Glos for Defendants and Appellants.

Law Office of Neal C. Swensen and Neal C. Swenson for Plaintiffs and Respondents.

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Defendants Remington Financial Group, Inc. (RFG), Andrew Bogdanoff, and Dan Gura challenge the trial court's order denying their petition to compel arbitration of the claims brought against them by plaintiffs Michelle's Diamond LLC (MDL), Cove Communities, Inc. (Cove), Mark Larson, Rooney Paul Masters, and JL Real Estate Investments (JLREI). Despite the parties' failure to fully execute the various agreements containing the subject arbitration clauses, defendants contend plaintiffs' breach of contract allegations in their complaint estop them from denying the enforceability of the arbitration clauses.

We conclude defendants have failed to meet their burden of demonstrating enforceable arbitration agreements. Although plaintiffs' operative complaint alleged breach of contract claims, it also alleged the contracts were illegal because defendants entered into them in violation of a desist and refrain order issued by the California Corporations Commissioner. Moreover, defendants' answer asserts the contracts are unenforceable against them because they are illegal and have not been executed by them. Accordingly, defendants may not rely on estoppel to meet their burden of demonstrating the existence of an enforceable arbitration agreement. Because defendants have provided no evidence in support of their petition to compel arbitration, we conclude the trial court did not err in denying the petition.

I

FACTUAL AND PROCEDURAL BACKGROUND

Plaintiffs sued defendants and Vantage Real Estate Solutions, Inc. (Vantage),¹ for damages under legal theories of (1) violation of the Racketeer Influenced and Corrupt Organizations Act (RICO), title 18 United States Code section 1961 et seq.; (2) breach of contract; (3) fraud; (4) negligent misrepresentation; (5) breach of fiduciary

¹ Although Vantage is a named defendant in the case, it is not part of this appeal.

duty; (6) negligence; (7) common counts (money had and received); (8) conversion; and (9) unfair competition (Bus. and Prof. Code § 17200). According to plaintiffs' operative second amended complaint, RFG, directed by Bogdanoff and Gura, engaged in a fraudulent scheme to obtain money from developers and other commercial loan customers by posing as a commercial lender and charging substantial advance fees without intending to provide or procure financing. The complaint further alleges that at the time RFG transacted business with plaintiffs, RFG was acting in violation of a desist and refrain order issued by the California Department of Corporations, based on the type of activities alleged in the complaint. The plaintiffs allege they paid money to RFG in connection with a series of written agreements, as follows:

A. *MDL*

MDL alleges it paid more than \$30,000 to RFG and Vantage pursuant to a letter of interest and term sheet to obtain a \$1 million loan. The letter of interest, between Vantage and "Michelle Diamonds LLC," is signed by Ingrid Robinson on behalf of Michelle Diamonds, but the signature line for Marcus Garcia as CEO of Vantage is unsigned. The letter of interest contains an arbitration clause calling for Arizona venue (AZ arbitration clause), which provides: "In the event of a dispute arising from the contemplated transaction between the parties that cannot be amicably resolved between the parties through reasonable diligent prior effort, parties hereby agree to binding arbitration in Maricopa County, AZ as the venue with sole jurisdiction. Any award will be limited to actual consideration paid, provided or due to the prevailing party."

The term sheet dated January 18, 2007, between RFG and MDL, is not signed by either party. The term sheet does not contain an arbitration clause.

B. *Cove*

Cove alleges it paid over \$30,000 in connection with two contracts and two letters of interest involving two projects in Long Beach, California. In the first contract,

Vantage promised to obtain \$40,000,000 financing for Cove's "Long Beach 138" project. Both parties signed the contract, which does not contain an arbitration clause.

The letter of interest between RFG and "Long Beach 138/14 Portfolio" is signed by the latter party, but unsigned by RFG. The letter of interest contains the AZ arbitration clause.

In the second contract, Vantage promised "5505 Ackerfield LLC" to obtain \$15,000,000 in financing in connection with the "Ackerfield Condo Conversions." The contract is signed by both parties and does not contain an arbitration clause.

The letter of interest between Vantage and "Long Beach Condo Conversion" relating to a proposed \$14,400,000 loan is signed by the latter party, but not by Vantage. The letter of interest contains the AZ arbitration clause.

C. *Larson*

Larson alleges he paid over \$25,000 for a letter of interest and term sheet on the "Blue Chairs Hotel" project. The letter of interest, dated April 10, 2007, between RFG and Larson is not signed by either party. The document contains the AZ arbitration clause.

The term sheet between RFG and Larson is not signed by either party. It contains an arbitration clause specifying venue in Pennsylvania, (PA arbitration clause) which provides: "In the event of a dispute arising from the contemplated transaction between the parties that cannot be amicably resolved between the parties through reasonable diligent prior effort, parties hereby agree to binding arbitration in Montgomery County, PA as the venue with sole jurisdiction. Any award will be limited to actual consideration paid, provided or due to the prevailing party."

D. *Masters*

Masters alleges he paid more than \$21,500 to RFG pursuant to a letter of interest and term sheet to obtain a \$2.6 million loan for his South Beach Vistas project.

The letter of interest attached to the complaint, dated May 9, 2007, is signed by Masters on behalf of South Beach Vistas. The signature line for Bogdanoff, as president of RFG, is unsigned. The letter of interest contains the AZ arbitration clause.

The term sheet attached to the complaint, dated June 13, 2007, references South Beach Vistas, but is signed by Masters on behalf of “Donovan, Ltd. a Belize company.” The term sheet is signed by Dan Gura, as “EVP” of RFG. The term sheet contains the PA arbitration clause.

E. *JLREI*

JLREI alleges it paid more than \$21,000 to RFG pursuant to a letter of interest and term sheet in an effort to obtain \$2.7 million acquisition financing. The letter of interest dated February 22, 2007, is signed by Bogdanoff as president of RFG and by JLREI. The letter of interest contains the AZ arbitration clause.

The term sheet dated April 3, 2007, is signed by JLREI, but the signature line for Bogdanoff or RFG is unsigned. The term sheet contains the PA arbitration clause.

Relying on the letters of interest and term sheets attached to the complaint, defendants filed a petition to compel all of the plaintiffs to arbitration in Arizona. The trial court denied the petition, and defendants now appeal.

II

DISCUSSION

Defendants May Not Rely On Plaintiffs’ Breach of Contract Allegations to Establish the Validity of the Arbitration Clauses While Asserting Defenses Based on Illegality and Lack of Execution

“‘A petition to compel arbitration “‘is in essence a suit in equity to compel specific performance of a contract.’” [Citations.]’ [Citation.]” (*City of Hope v. Bryan Cave, L.L.P.* (2002) 102 Cal.App.4th 1356, 1369 (*City of Hope*)). “[I]n circumstances

generally involving contractual arbitration provisions, when a petitioner files a petition to compel arbitration of that arbitration provision, a trial court must make preliminary factual determinations whether: (1) there is an arbitration agreement; and (2) the petitioner is a party to that agreement or can otherwise enforce that agreement.

[Citation.] Code of Civil Procedure section 1281.2 authorizes petitions to compel arbitration, providing in part: ‘On petition of a *party to an arbitration agreement* alleging the existence of a written agreement to arbitrate a controversy and that a party thereto refuses to arbitrate such controversy, the court shall order the petitioner and the respondent to arbitrate the controversy *if it determines that an agreement to arbitrate the controversy exists . . .*’ [Italics added.] Therefore, in considering a Code of Civil Procedure section 1281.2 petition to compel arbitration, a trial court must make the preliminary determinations whether there is an agreement to arbitrate and whether the petitioner is a party to that agreement (or can otherwise enforce the agreement).

[Citation.] [¶] ‘As a general matter, only signatories to an arbitration agreement may enforce it. [Citation.]’ [Citation.] However, there are exceptions to that general rule for nonsignatory persons who are agents or alter egos of a signatory party or intended third party beneficiaries of an arbitration agreement.” (*Bouton v. USAA Cas. Ins. Co.* (2008) 167 Cal.App.4th 412, 424.)

“The petitioner bears the burden of proving the existence of a valid arbitration agreement by the preponderance of the evidence, and a party opposing the petition bears the burden of proving by a preponderance of the evidence any fact necessary to its defense. [Citation.] In these summary proceedings, the trial court sits as a trier of fact, weighing all the affidavits, declarations, and other documentary evidence, as well as oral testimony received at the court’s discretion, to reach a final determination. [Citation.]” (*Engalla v. Permanente Medical Group, Inc.* (1997) 15 Cal.4th 951, 972 (*Engalla*).)

In support of their petition, defendants submitted the declaration of Steven M. Dailey, their defense and appellate counsel. Dailey's declaration attaches the letters of interest and term sheets that plaintiffs attached to their third amended complaint. Other than noting the documents are attached to plaintiffs' complaint, Dailey's declaration provides no evidence demonstrating whether the documents are authentic or enforceable against defendants. Defendants therefore rely exclusively on plaintiffs' complaint and attachments to demonstrate the existence of enforceable arbitration agreements. Recognizing that many of the agreements were not fully executed, defendants contend the complaint's breach of contract allegations constitute binding judicial admissions that the contracts are enforceable. We disagree.

“[A]n admission in a pleading is *conclusive* on the pleader.” (*Valerio v. Andrew Youngquist Construction* (2002) 103 Cal.App.4th 1264, 1272.) Here, each of the plaintiffs relies on at least one agreement containing an arbitration clause for its breach of contract claims. Moreover, the plaintiffs' other causes of action arise from the obligations outlined in these agreements. Although some of the contracts are between one of the plaintiffs and Vantage, plaintiffs alleged in their complaint that “Vantage acted as a surrogate for RFG.” The complaint further alleges that Gura and Bodanoff directed RFG's activities, and that “each of the defendants were the agents and/or employees of each of the other defendants, and . . . were acting within the scope of that agency and employment” Thus, at first blush, plaintiffs' allegations appear to support defendants' petition to compel arbitration.

But unlike the usual situation in which a plaintiff alleging a breach of contract asserts the validity of the contract, plaintiffs here allege the contracts are illegal. Specifically, the complaint alleges RFG was subject to a desist and refrain order issued by the California Department of Corporations Commissioner, who declared the types of agreements at issue here to be unlicensed securities. RFG's agreements with plaintiffs violated the order and therefore defendants could not enforce the contracts. “Section

1281 of the Code of Civil Procedure, providing for submission to arbitration of ‘any controversy . . . which arises out of a contract,’ does not contemplate that the parties may provide for the arbitration of controversies arising out of contracts which are expressly declared by law to be illegal and against the public policy of the state.” (*Loving & Evans v. Blick* (1949) 33 Cal.2d 603, 610.) Accordingly, whether a contract as a whole is illegal is a matter to be decided by the courts, not the arbitrator. (*Hotels Nevada, LLC v. Bridge Banc, LLC* (2005) 130 Cal.App.4th 1431, 1436.)²

Defendants also argue that principles of estoppel prevent plaintiffs from asserting breach on contract claims while opposing enforcement of the arbitration provisions in the contracts underlying those claims. Again, we disagree.

“‘Equitable estoppel precludes a party from asserting rights “he otherwise would have had against another” when his own conduct renders assertion of those rights contrary to equity.’ [Citation.] In the arbitration context, a party who has *not* signed a contract containing an arbitration clause may nonetheless be compelled to arbitrate when he seeks enforcement of other provisions of the same contract that benefit him.

[Citations.] . . . [¶] [A] plaintiff who ‘ultimately must rely on the terms of [an] agreement in its claims against the [nonsignatory defendant]’ should be ‘equitably estopped from repudiating the arbitration clause of the agreement.’ [Citation.] ‘[A party is] not entitled to make use of the [contract containing an arbitration clause] as long as it worked to her advantage, then attempt to avoid its application in defining the forum in

² The contracts’ illegality, however, does not necessarily prevent *plaintiffs* from enforcing them. Although courts generally withhold relief under a contract that is illegal or violates public policy, this general rule is “‘intended to prevent the guilty party from reaping the benefit of his wrongful conduct’” (*Maudlin v. Pacific Decision Sciences Corp.* (2006) 137 Cal.App.4th 1001, 1013.) Thus, “““In some cases, . . . effective deterrence is best realized by enforcing the plaintiff’s claim rather than leaving the defendant in possession of the benefit; or the forfeiture resulting from unenforceability is disproportionately harsh considering the nature of the illegality. In each case, how the aims of policy can best be achieved depends on the kind of illegality and the particular facts involved.”” [Citation.]” (*Ibid.*)

which her dispute . . . should be resolved.’ [Citation.] The doctrine thus prevents a party from playing fast and loose with its commitment to arbitrate, honoring it when advantageous and circumventing it to gain undue advantage.” (*Metalclad Corp. v. Ventana Environmental Organizational Partnership* (2003) 109 Cal.App.4th 1705, 1713-1714 (*Metalclad*) [analyzing estoppel under federal law]; see also *Rowe v. Exline* (2007) 153 Cal.App.4th 1276, 1288 [applying federal estoppel principles in *Metalclad* to resolve arbitration disputes under California law].)

But estoppel is, by definition, an equitable doctrine. Defendants do not admit they are bound by the agreements. Indeed, Dailey’s declaration in support of defendants’ petition appears carefully worded to avoid attesting to the validity of the documents attached to the second amended complaint. Significantly, in their answer filed six days before the trial court’s order denying arbitration, defendants asserted affirmative defenses alleging the agreements are unenforceable because, inter alia, they are illegal and have not been signed by the defendants.³ In essence, defendants seek to specifically enforce the arbitration provisions in the agreements while at the same time challenging the validity of those same contracts.

The defendants’ situation is similar to the defendants in the recent case of *Brodke v. Alphatec Spine Inc.* (2008) 160 Cal.App.4th 1569, in which the defendants attempted to compel arbitration based upon a contractual provision. The defendants, however, failed to allege the validity of the contracts containing the provision, and instead relied on the plaintiffs’ breach of contract allegations in their complaint. Defendants argued in part that the equitable estoppel principles we enunciated in *Metalclad* required arbitration based solely on the plaintiffs’ allegations. We rejected this argument, observing that “*Metalclad* does not stand for the proposition that a party

³ Specifically, defendants’ answer asserts that plaintiffs’ breach of contract claims are barred “by the doctrine of illegality of contract,” and because the agreements “were required by law to be in writing and signed by the party to be charged.”

petitioning to enforce an arbitration clause may simultaneously deny the existence of the very contract sought to be enforced.” (*Brodke*, at p. 1575.)

Similarly, in *City of Hope, supra*, 102 Cal.App.4th 1356, a medical center sued its former attorney and law firm alleging the defendants breached their fiduciary duties to the plaintiff by assisting the plaintiff’s former officers in preparing secret agreements harmful to the plaintiff’s interests. The plaintiff amended its complaint to include allegations the defendants had acted as agents of the former officers. Because the settlement agreements plaintiff had reached with the former officers purported to cover the former officer’s agents, defendants sought to compel arbitration based on the complaint’s new agency allegations. The court rejected this attempt, observing: “[T]he linchpin of equitable estoppel is fairness. Here, there is no fairness principle upon which [defendants] can rely. Both [defendants] deny they were ever the agents of the Former Officers, just as they deny they ever did anything wrong in their representations of [plaintiff].” (*Id.* at pp. 1370-1371.) The court concluded the defendants “tried to finesse their way into arbitration” without providing any proof they could invoke the arbitration provisions of the former officers’ settlement agreements. (*Id.* at p. 1371.)

Finally, in *Berman v. Renart Sportswear Corp.* (1963) 222 Cal.App.2d 385, 389, the sales representative plaintiff sued his employer, claiming breach of an oral agency agreement that was formed after a written agreement had expired. The plaintiff’s complaint alleged the defendant had denied the existence of the oral agreement. The defendant, without answering the complaint, filed a petition to compel arbitration asserting that plaintiff’s alleged oral agreement would be an extension of the written agreement that contained an arbitration clause. The appellate court upheld denial of the petition to compel arbitration, observing: “The record . . . shows a positive allegation by plaintiff that appellant had denied the existence of the oral agreement involved This allegation has never been denied by appellant. Its petition for arbitration did not allege any extension of the original written contract, but merely set forth that there were

‘alleged’ extensions or renewals thereof. This is not enough. *Appellant must take a positive position, in the trial court, as to the several allegations of the complaint. Until it does so, neither the trial court, nor we, can determine whether or not a contract to arbitrate exists . . .*” (*Berman*, at p. 389, italics added.)

Defendants contend plaintiffs failed to prove the contracts at issue are illegal because the desist and refrain order attached to the complaint was not authenticated, and was unsigned by the California Department of Corporations Commissioner. We agree the unauthenticated and unsigned desist and refrain order by itself is insufficient to meet plaintiffs’ “burden of proving by a preponderance of the evidence any fact necessary to its defense.” (See *Engalla*, *supra*, 15 Cal.4th at p. 972.) But defendants bear the initial “burden of proving the existence of a valid arbitration agreement by the preponderance of the evidence . . .” (*Ibid.*) Defendants produced no evidence, and chose instead to rely exclusively on plaintiffs’ complaint and estoppel principles. Defendants, however, disregard the complaint’s allegations that the contracts are illegal, and their own defenses that the contracts are not enforceable because they are illegal and unsigned by them. Defendants’ attempt to specifically enforce the arbitration clauses in the agreements alleged in the complaint, while disclaiming the remainder of the agreements’ provisions, is the type of “fast and loose” play the equitable estoppel doctrine was designed to prevent. (See *Metalclad*, *supra*, 109 Cal.App.4th at p. 1714.) Unable to rely on estoppel, defendants have failed to meet their burden of demonstrating the existence of an enforceable arbitration agreement. Consequently, plaintiffs’ burden to establish a defense to arbitration did not arise. We therefore conclude the trial court did not err in denying defendants’ petition to compel arbitration.

III

DISPOSITION

The order is affirmed. Plaintiffs are awarded their costs of this appeal.

ARONSON, J.

WE CONCUR:

BEDSWORTH, ACTING P. J.

IKOLA, J.